No. 80-1256

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In the Supreme Court of the United States

OCTOBER TERM, 1980

MARIE D. NESBITT, PETITIONER

v.

UNITED STATES OF AMERICA, ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

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QUESTION PRESENTED

Whether the priority under Section 3466 of the Revised Statutes for "the debts due to the United States" from an insolvent person defeats the lien of a judgment creditor under 26 U.S.C. 6323(a), as amended by the Federal Tax Lien Act of 1966, where the judgment lien was filed prior to the federal tax lien and the insolvency of the debtor, but the judgment creditor failed to enforce her lien by execution.

TABLE OF CONTENTS

Page

Opinions below 1

Jurisdiction 1

Statute and regulations involved 1

Statement 2

Argument 3

Conclusion 8

TABLE OF AUTHORITIES

Cases:

H.B. Agsten & Sons, Inc. v. *Huntington Trust & Savings Bank*, 388 F. 2d 156 7

Commonwealth v. *Covil*, 474 Pa. 375, 378 A.2d 841 8

Commonwealth v. *Davenport*, 462 Pa. 543, 342 A.2d 67 8

Commonwealth v. *Rightnour*, 469 Pa. 107, 364 A.2d 927 8

Commonwealth of Kentucky, Department of Revenue v. *United States*, 383 F. 2d 13 7

Decker's Estate, In re, 355 Pa. 331, 49 A.2d 714, cert. denied, 331 U.S. 807 7-8

Estate of Adolph P. Berretta, In re, Nos. 11, 12 (Pa. Mar. 13, 1981) 8

Exchange Bank & Trust Co. v. *Tubbs Mfg. Co.*, 246 F. 2d 141, cert. denied, 355 U.S. 868 8

National Surety Corp. v. *Sharpe*, 236 N.C. 35, 72 S.E.2d 109 7

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Page

Cases—(Continued):

New York v. *Maclay*, 288 U.S. 290 ..... 4, 8

Sapero v. *O'Connell*, No. 799 (Md. Ct. Spec. App. Mar. 13, 1981) 7

Thelusson v. *Smith*, 15 U.S. (2 Wheat.) 396 4

United States v. *Emory*, 314 U.S. 423 4

United States v. *Gilbert Associates*, 345 U.S. 361 4

United States v. *Kimbell Foods, Inc.*, 440 U.S. 715 5

United States v. *Moore*, 423 U.S. 77 3-4

United States v. *New Britain*, 347 U.S. 81 5

United States v. *South Carolina*, 227 S.C. 187, 87 S.E.2d 577 7

United States v. *Vermont*, 377 U.S. 351 ..... 3, 5

Statutes:

Act of Mar. 3, 1797, ch. 20, Section 5, 1 Stat. 515 3

Act of Mar. 4, 1913, ch. 166, 37 Stat. 1016 6

Federal Tax Lien Act of 1966, Pub. L. No. 89-719, Section 101(a), 80 Stat. 1125 6

Page

Statutes—(Continued):

Internal Revenue Code of 1954 (26 U.S.C.):

Section 6323 ..... 5, 6, 7
Section 6323(a) 1, 2, 4, 6, 7

Rev. Stat. 3186 6

Rev. Stat. 3466, 31 U.S.C.
191 ..... 1, 2, 3, 4, 5, 6, 7, 8

Miscellaneous:

ABA, *Final Report of the Committee on Federal Liens* (1959) 6

105 Cong. Rec. (Index) (1959):

p. 1030 6

p. 1258 6

117 Cong. Rec. 1650 (Index) (1971) 7

H.R. Rep. No. 1018, 62d Cong., 2d Sess. (1912) 6

H.R. Rep. No. 1884, 89th Cong., 2d Sess. (1966) 6

Priority of Federal Tax Liens and Levies: Hearings on H.R. 11256 and H.R. 11290 Before the House Comm. on Ways and Means, 89th Cong., 2d Sess. (1966) 6, 7

S. 2197, 92d Cong., 1st Sess. (1971) 7

S. Rep. No. 1708, 89th Cong., 2d Sess. (1966) 6

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OPINIONS BELOW

The opinion of the district court (Pet. App. 4A-34A) is reported at 445 F. Supp. 824. The opinion of the court of appeals (Pet. App. 1A-3A) is reported at 622 F. 2d 433.

JURISDICTION

The judgment of the court of appeals was entered on June 26, 1980 (Pet. App. 35A-36A), and a petition for rehearing was denied on October 2, 1980 (Pet. App. 37A-38A). By order dated December 15, 1980, Mr. Justice Rehnquist extended the period in which to file a petition for a writ of certiorari to January 23, 1981, and the petition was filed on that date. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATUTE AND REGULATIONS INVOLVED

The pertinent provisions of Rev. Stat. 3466, 31 U.S.C. 191 and Section 6323(a) of the Internal Revenue Code of 1954 (26 U.S.C.) are set forth at Pet. App. 39A-66A.

STATEMENT

The question presented in this federal income tax collection case involves the resolution of the competing claims of petitioner, a judgment creditor, and the United States, against the net proceeds of the sale of real property of an insolvent debtor.

The pertinent facts are undisputed and may be summarized as follows: The United States assessed tax liabilities against the debtor, Franklyn K. Brann, who died on May 26, 1976, in the amount of $89,160.06 for income taxes for 1974, 1975, and 1976, and for withholding and F.I.C.A. taxes for the taxable periods ending December 31, 1974, March 31, 1975, June 30, 1975, September 30, 1975, March 31, 1976, and June 30, 1976 (R. 28-30).[1] On September 7, 1976, January 17 and 25, 1977, the Internal Revenue Service filed notices of tax liens in the aggregate amount of $55,872.72. Petitioner holds a default judgment against Brann in the amount of $225,061 which she recorded on April 28, 1976. However, petitioner never executed on her judgment (Pet. App. 6A-7A, 27A).

At the time of his death, the debtor Brann and his wife owned an individual 13% interest in real property. That interest was sold pursuant to agreement of the parties, and the proceeds are being held for distribution as determined in this proceeding. It is agreed that the decedent's estate is insolvent, *i.e.*, "insufficient to pay all the debts due from the deceased" within the meaning of Rev. Stat. 3466, 31 U.S.C. 191 (Pet. App. 6A-9A, 11A).

Petitioner brought this action in the United States District Court for the Northern District of California seeking a determination that her claims as a judgment creditor under 26 U.S.C. 6323(a) to certain proceeds from the sale of the debtor's real property had priority over the tax claims of the

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[1] "R." refers to the record in the court of appeals.

United States under Rev. Stat. 3466, 31 U.S.C. 191. The district court upheld the priority of the government's tax claim. After reviewing the authorities, it concluded that "a lien, including a judgment lien, will only be excepted from the operation of §3466 if it has been reduced to possession, thereby divesting the judgment debtor of either title or possession" (Pet. App. 32A). Even on the assumption that perfected and specific liens are excepted from the rule of absolute priority established by Section 3466 (a question the district court declined to address), the court concluded that "[petitioner's] lien, not being sufficiently perfected and specific, does not qualify under such an exception" (Pet. App. 33A). The court of appeals affirmed for the reasons stated in the district court's opinion (Pet. App. 1A-3A).

ARGUMENT

The decision below correctly held that the government's tax claim under Section 3466 of the Revised Statutes against an insolvent estate had priority over petitioner's unperfected judgment lien.

1. Section 3466 of the Revised Statutes, 31 U.S.C. 191, provides in pertinent part that "[w]henever any person indebted to the United States is insolvent, or whenever the estate of any deceased debtor, in the hands of the executors or administrators, is insufficient to pay all the debts due from the deceased, the debts due to the United States shall be first satisfied * * *."

The statute has its roots in the early enactments of the Republic, *i.e.*, the Act of Congress of Mar. 3, 1797, ch. 20, Section 5, 1 Stat. 515. By its broad terms, it admits of no exceptions in conferring absolute priority for debts due the United States from an insolvent person or estate. *United States* v. *Vermont*, 377 U.S. 351, 357 (1964). As the Court recently affirmed, " '[o]nly the plainest inconsistency would warrant our finding an implied exception to the operation of so clear a command as that of §3466.' " *United States* v.

Moore, 423 U.S. 77, 82-83 (1975), quoting from *United States* v. *Emory*, 314 U.S. 423, 433 (1941). Accordingly, if the insolvent debtor is in possession of property, the priority of Section 3466 defeats unexecuted judgment liens. As the Court held more than 150 years ago in *Thelusson* v. *Smith*, 15 U.S. (2 Wheat.) 396, 426 (1817), "the general lien of a judgment upon the lands of an insolvent debtor is subordinate to the preference established by the statute unless seizure by a marshal or some other equivalent act has made the lien specific and brought about a change of title or possession." *New York* v. *Maclay*, 288 U.S. 290, 293-294 (1933).

Moreover, Section 3466 applies to all the insolvent's debts to the government, whether or not arising from taxes, and whether or not secured by a lien. In *United States* v. *Gilbert Associates*, 345 U.S. 361, 366 (1953), the Court accorded priority under the statute to subsequently arising claims of the United States against an insolvent debtor even though the identity of a prior existing lienor, the amount of the lien, and the property subject to the lien were all clearly established. As the Court observed, "[i]n claims of this type, 'specificity' requires that the lien be attached to certain property by reducing it to possession, on the theory that the United States has no claim against property no longer in the possession of the debtor * * *. The taxpayer has not been divested by the Town of either title or possession. The Town, therefore, had only a general, unperfected lien" (*id.* at 366). Here, too, petitioner's competing lien did not reduce the debtor's property to her possession. The court of appeals therefore correctly concluded that petitioner's lien was "not sufficiently perfected and specific to come within any such exception [to Section 3466]" (Pet. App. 3A).

2. Petitioner's claim to priority for her unperfected judgment lien rests upon Section 6323(a) of the Internal Revenue Code of 1954 (26 U.S.C.), as amended by the

Federal Tax Lien Act of 1966. That statute provides that federal tax liens "shall not be valid as against any purchaser, holder of a security interest, mechanic's lienor, or judgment lien creditor until notice thereof which meets the requirements of subsection (f) has been filed by the Secretary." Since petitioner's judgment lien was recorded prior to the filing of the federal tax lien of the United States, she claims priority under Section 6323. In petitioner's view, that provision overrides the rule of absolute priority in favor of the government provided by Section 3466 of the Revised Statutes. In support of this argument, petitioner cites this Court's decision in *United States* v. *Kimbell Foods, Inc.*, 440 U.S. 715 (1979).

But Section 6323 has no application to a case where, as here, the debtor is insolvent and the government's claim derives from Section 3466 of the Revised Statutes. Petitioner's claim under Section 6323 would be accorded priority if the government's claim derived from an after-arising tax lien. As this Court stated in *United States* v. *Vermont, supra*, 377 U.S. at 358, it is "quite clear that different standards apply where the United States' claim is based on a tax lien arising under §§6321 and 6322 (footnote omitted)." See also *United States* v. *New Britain*, 347 U.S. 81 (1954).

Nor does *United States* v. *Kimbell Foods, Inc., supra*, require a different result. There, the Court held that in the absence of a federal statute setting priorities, a uniform national rule was unnecessary to protect the federal interests underlying federal loan programs with respect to the question whether contractual liens arising from the loan programs take precedence over private liens. The Court accordingly adopted state law as the appropriate federal rule for establishing the relative priority of these competing federal and private liens. Here, on the other hand, Congress has long evidenced its intention in Section 3466 to establish a uniform national rule of absolute priority in favor of the

federal government for its claims against insolvent debtors. *Kimbell Foods, Inc.* therefore has no application to this case.

There is, moreover, no basis for petitioner's suggestion (Pet. 27-30) that Congress intended to modify Section 3466 by the amendments to Section 6323 of the Code contained in Section 101(a) of the Federal Tax Lien Act of 1966, Pub. L. No. 89-719, 80 Stat. 1125. Section 3186 of the Revised Statutes, the antecedent of Section 6323(a), was amended by the Act of Mar. 4, 1913, ch. 166, 37 Stat. 1016, to accord a mortgagee, purchaser, or judgment creditor priority over a federal tax lien. However, nothing in the underlying legislative history of that enactment or of the 1966 legislation diminishes the Section 3466 priority of the United States in insolvency. H.R. Rep. No. 1018, 62d Cong., 2d Sess. (1912); H.R. Rep. No. 1884, 89th Cong., 2d Sess. (1966); S. Rep. No. 1708, 89th Cong., 2d Sess. (1966).

Indeed, Congress has refused to enact proposals which would have explicitly narrowed the sweep of Section 3466 in the circumstances of this case. For example, in 1959, the American Bar Association proposed a modification of Section 3466 to protect the validity of a "lien or security interest which would have been entitled to priority over the claim of the United States immediately preceding such divestment [of title or possession]" (ABA, *Final Report of the Committee on Federal Liens* 122 (1959) *reprinted in Priority of Federal Tax Liens and Levies: Hearings on H.R. 11256 and H.R. 11290 Before the House Comm. on Ways and Means*, 89th Cong., 2d Sess. 197 (1966) (hereinafter cited as "*House Hearings*")). Although a bill to this effect was introduced in the 86th Congress, it was not reported out of committee. See 105 Cong. Rec. 1030, 1258 (Index) (1959). Moreover, this proposal was again presented to Congress during its consideration of the Federal Tax Lien Act of 1966 (see

House Hearings, supra, at 75-88, 196-201). Neither Section 3466 nor Section 6323 of the Code was so altered.[2] In light of the statement in the American Bar Association's Report that the proposed provision "would assure, contrary to the suggestions made in some decisions, that any lien which would qualify for priority in the absence of insolvency would continue to enjoy such priority" (see *House Hearings, supra*, at 199), Congress' refusal to adopt the ABA proposal lends further support to the correctness of the decision below.

3. Contrary to petitioner's final argument (Pet. 17-20), there is no present conflict of decisions with respect to the question presented requiring resolution by this Court. In *Sapero* v. *O'Connell*, No. 799 (Mar. 13, 1981), the Maryland Court of Special Appeals recently concluded, in conformity with the decision below, that the priority in favor of the United States under Section 3466 was unaffected by those provisions governing unexecuted judgment lien creditors under Section 6323(a), as amended by the Federal Tax Lien Act of 1966. Accord: *H.B. Agsten & Sons, Inc.* v. *Huntington Trust & Savings Bank*, 388 F. 2d 156, 160 (4th Cir. 1967) (Haynsworth, J., concurring). Although the decisions are not uniform under the pre-1966 law,[3] no appellate

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[2]A revised version of the American Bar Association's insolvency priority recommendation was before the Senate Judiciary Committee in 1971 as S. 2197, 92d Cong., 1st Sess. This bill likewise was not reported out of committee. See 117 Cong. Rec. 1650 (Index) (1971).

[3]See *Commonwealth of Kentucky, Department of Revenue* v. *United States*, 383 F. 2d 13 (6th Cir. 1967) (government's priority under Section 3466 defeats judgment lien creditor). Contra: *National Surety Corp.* v. *Sharpe*, 236 N.C. 35, 72 S.E.2d 109 (1952); *United States* v. *South Carolina*, 227 S.C. 187, 87 S.E.2d 577 (1955).

Despite some language at odds with the analysis of the court below in this case, the other cases upon which petitioner relies (Pet. 19-20) are distinguishable. In *In re Decker's Estate*, 355 Pa. 331, 49 A.2d 714

court has upheld petitioner's contention that an unperfected prior judgment lien arising under the Federal Tax Lien Act of 1966 defeats the absolute priority of the United States under Section 3466 of the Revised Statutes.[4]

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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APRIL 1981

(1946), cert. denied, 331 U.S. 807 (1947), the competing claimants were pledgees who, prior to the insolvency, *possessed* the stock which was the subject of the controversy. *Exchange Bank & Trust Co.* v. *Tubbs Mfg. Co.*, 246 F. 2d 141 (5th Cir.), cert. denied, 355 U.S. 868 (1957), concerned the competing interests of the government and mortgagees. In both *Decker's Estate* and *Exchange Bank* the competing claimants arguably had attained the requisite "title or possession." See *New York* v. *Maclay*, *supra*, 288 U.S. at 293-294.

[4]In *In re Estate of Adolph P. Berretta*, Nos. 11, 22, (Mar. 13, 1981), the Supreme Court of Pennsylvania affirmed by an equally divided court a decision in favor of a prior judgment lienor over a claim of the United States under Section 3466. This decision, however, has no binding precedential value as a ruling on the merits. See *Commonwealth* v. *Rightnour*, 469 Pa. 107, 364 A.2d 927 (1976); *Commonwealth* v. *Covil*, 474 Pa. 375, 378 A.2d 841 (1977); *Commonwealth* v. *Davenport*, 462 Pa. 543, 559 n.3, 342 A.2d 67, 75 n.3 (1975).